**Before the**
**FEDERAL COMMUNICATIONS COMMISSION**
**Washington, D.C. 20554**

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| In the Matter of<br><br>Developing a Unified Intercarrier<br>Compensation Regime | CC Docket No. 01-92 |

# COMMENTS OF VERIZON


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### Summary

It is timely for the Commission to make an overall assessment of the various intercarrier compensation mechanisms that exist in the industry today.[2] These mechanisms have developed independently over the course of more than twenty years, sometimes in response to specific congressional direction and often without regard to the way each one might interact with another. Because of the changes in the marketplace brought about by technical advancements and by the 1996 Act, a comprehensive review at this juncture is especially appropriate.

The most far reaching proposal would scrap various local and access intercarrier compensation arrangements and replace them with a bill-and-keep regime. While such a change might simplify the current arrangements, the Commission should not jump into such a major shift without carefully analyzing the results and thinking through all the possible ramifications. As the Commission and the industry learned from the experience with reciprocal compensation for Internet-bound calls, clever providers can game compensation systems for their own personal benefit to the detriment of consumers and the industry overall. And as that same experience also

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[1] The Verizon telephone companies are the local exchange and interexchange carriers affiliated with Verizon Communications Inc., listed in Attachment A.

teaches us, once established, it is very difficult to put such arrangements to an end. As large as the Internet-bound problem was — totaling approximately $2 billion per year[3] — replacing access and local compensation generally with bill-and-keep could result in even greater opportunities for uneconomic activity. Any action by the Commission, therefore, must be carefully thought through in order to avoid such problems. The Commission should put a plan in place to study the implications of any proposed changes with extended opportunity for public comment and review.

There are, however, issues that the Commission has recognized that can and should be addressed now. First, it should finish the job it started in the *Reciprocal Compensation Remand Order* and move all Internet-bound traffic to bill-and-keep. Second, it should put an end to LECs' fraudulent use of telephone numbers to game the existing system and effectively steal free service by disguising toll calls as local calls. Third, the Commission should address the problems that are being caused today when one carrier attempts to make another carrier unfairly bear the cost of its network architecture design.

After dealing with these near-term issues, the Commission should turn to the bigger questions of whether there should be a single intercarrier compensation regime and, if so, what that regime should be. In considering these questions, the Commission should be guided by a few overarching principles. First, it should allow market-based arrangements, negotiated by the participants. Mandatory regulatory defaults should be available as an alternative. Second, intercarrier compensation must not be blindly based on technologies (circuit-switched, packet-

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[2] *Developing a Unified Intercarrier Compensation Regime*, Notice of Proposed Rulemaking, CC Docket No. 01-92, FCC 01-132 (rel. April 27, 2001) ("*Notice*").

[3] *Intercarrier Compensation for ISP-Bound Traffic*, CC Docket Nos. 96-98 and 99-68, FCC 01-131 at ¶ 5 (rel. Apr. 27, 2001) ("*Remand Order")*.

switched and the next generation), the transport medium (wireline, wireless, cable, radio/microwave, satellite, electric, cable networks, etc.), or what regulatory category the service provider falls under (ILEC, CLEC, CMRS provider, paging, IXC, cable operator, etc.). There should be only rational distinctions based on real differences in technology or law. Third, any new intercarrier compensation system should encourage facilities-based market entry and expand the number of options available to the consumers.

**1. The Near-Term Issues**

A. The Commission Should Fully Eliminate the Arbitrage on Internet-Bound Calls.

In the *Remand Order*, the Commission found that the extraction of reciprocal compensation for Internet-bound calls was "regulatory arbitrage" that "distorted the economic incentives related to competitive entry into the local exchange and exchange access markets."[4] For that reason, it promptly cut off new opportunities for carriers to engage in these activities — "our goal here is to address and curtail a pressing problem that has created opportunities for regulatory arbitrage and distorted the operation of competitive markets" and "seek to confine these market problems to the maximum extent."[5] It did so, however, with only "an interim intercarrier compensation regime for ISP-bound traffic" that only serves to "limit" the opportunity for regulatory arbitrage.[6]

In this proceeding, the Commission should put this regulatory arbitrage to an end for good. A subset of carriers are still receiving hundreds of millions of dollars in payments from carriers of originating traffic for these calls, payments that are not necessary to permit the recipients to recover their costs. Moreover, these payments more than compensate the carriers

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4 *Remand Order* at ¶ 2.

5 *Remand Order* at ¶ 81.

receiving these payments because the record before the Commission demonstrates that these carriers' cost to terminate a call to an ISP is far less than the cost to terminate a call on a network that serves diverse and dispersed customers.[7] There is no legitimate policy reason all carriers cannot recover their costs just as Verizon does — from their customers. The answer is to do away with these payments, and the Commission should bring this transition period to an end as soon as possible and confirm that bill-and-keep is the rule for ISP-bound calls.[8]

B. The Commission Should Eliminate Fraudulent Misuse of Telephone Numbers.

Some LECs are misusing telephone numbers to make toll calls look like direct dial local calls.[9] This is not merely inefficient and another case of regulatory arbitrage; such fraudulent misuse of numbers effectively steals service from other carriers. It deprives the originating carrier of toll or access revenues and may require the originating carrier to pay compensation to the terminating LEC (which, of course, is one of the reasons the terminating LEC did it in the first place). The Commission should make it clear that these arrangements are unlawful. Even if the Commission were to conclude that this is a legitimate use of telephone numbers, this use does not transform a call that goes from one rate area to another into a local call.

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6 *Remand Order* at ¶ 77.

7 *E.g.*, *Ex parte* letter to Ms. Magalie Roman Salas from Robert T. Blau of BellSouth, CC Docket No. 99-68, dated Feb. 1, 2001, at 2-3 ("... the CLECs average switching costs for dial up traffic works out to about $.0001 per minute or about 1 to 5 percent of current reciprocal compensation rates"); *Ex parte* letter to Ms. Magalie Roman Salas from Gary L. Phillips of SBC Telecommunications, Inc., CC Docket No. 99-68, dated Feb. 16, 2001, at 1 ("significantly less than $.001") and attached Morgan Stanley Dean Witter In Depth Report at page 9, which states that soft-switches can be almost 70% cheaper than circuit-based technology.

8 This would not resolve the question of the appropriate compensation regime for Internet telephony calls. *See Federal-State Joint Board on Universal Service*, Report to Congress, 13 FCC Rcd 11501 at ¶ 90 (1998).

9 In paragraph 115, the *Notice* refers to this as "virtual central office codes."

This is a problem that the Commission can address now. When the Commission sets into place longer-term rules with an overall competitively neutral framework for intercarrier compensation, carriers will have less incentive to engage in such behavior. However, until such an overall plan is put into place, this inefficient behavior is distorting investment and market entry decisions, and can easily be stopped.

**The Theft of Service Schemes**. The way these schemes work is as follows: A LEC applies to the North American Numbering Plan Administrator (NANPA) for a block of telephone numbers, either an entire exchange (NXX) code of 10,000 numbers or a block of 1000 numbers in areas where thousands-block number assignment has been introduced. At that time, that carrier indicates the ILEC rate area for which the numbers are to be associated. The carrier, however, has no facilities in the rate area it designates, has no intention of trying to serve any customers who are located there, and may not interconnect with the ILEC in that area. The carrier then assigns these telephone numbers to customers, preferably customers with large volumes of in-coming calls, located outside the rate area, even hundreds of miles away on the other side of the state or in a different state altogether. To the originating carrier switch, calls to these numbers from customers in the rate area designated by the terminating carrier appear to be local — both the caller's telephone number and telephone number being called are associated with the same rate area. The originating carrier, therefore, does not treat the call as a long distance call and hand it off to the customer's presubscribed carrier. Because the call appears to be local, the originating carrier transports it to the terminating carrier's interconnection point and pays compensation to the terminating carrier. The terminating carrier gets the equivalent of an inbound 800 service for free, and then even gets paid for such fraud.

These arrangements also create disincentives for LECs to build their own facilities — why invest in a network when you can offer these long distance services merely by obtaining telephone numbers and having another carrier perform your transport. Many LECs have invested in networks to provide 800 and other toll-free services. But such facilities-based competition would be undermined if others are allowed to obtain the same benefit without investing in their own networks. No one could enter this market, build facilities and compete with carriers who obtain the use of another LEC's facilities without paying for them.

Finally, these schemes directly harm the originating carrier in three ways — the originating LEC loses either the toll or access revenues it would normally collect on these interexchange calls, it incurs costs to transport the call to the terminating carrier, and the originating LEC pays the terminating LEC reciprocal compensation.

As the *Notice* recognizes,[10] arrangements like this are not just a theoretical possibility — they are happening all over the country. One of the first cases to surface was in Maine, where Brooks Fiber (now part of WorldCom) obtained full NXX codes in more than 50 rate areas (more than half a million telephone numbers in all) and assigned them to customers in the Portland rate area, the only area in which it was even authorized to provide local service.[11] Brooks then offered an inbound-only, "toll-free" calling service to a select market segment, businesses which wanted their customers to be able to call them for long periods of time without either the originating (calling) or terminating (called) customer incurring any toll charges — and they wanted to do this without actually establishing a physical presence in each of the local

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[10] *Notice* at ¶ 115.

calling areas. As that agency concluded, "Brooks was instead using the NXX codes for the purpose of providing an interexchange service" and was doing so by using another carrier's services without paying for them.[12] Similarly,

> what Brooks is attempting to do is offer free incoming long distance *interexchange* service to customers of ILECs who are outside Portland and who want to call Brooks's customers in Portland. … *Our objections are to the use of 54 NXX codes to accomplish that end, when reasonable alternatives exist; and to the notion that Brooks is somehow entitled to use the facilities of someone else, for free, to accomplish that goal.* When a carrier uses facilities of others, it cannot unilaterally redefine wholesale arrangements between itself and the carriers that actually carry its traffic simply by declaring that its calls are 'local' if that recharacterization is to its financial advantage.[13]

After many months of litigation, the Maine commission put a stop to this practice.[14]

Moreover, these schemes are not just confined to intrastate arrangements. Carriers with no local customers in a state have sought and received local numbers in that state. As a result, calls to these numbers, which should legitimately be subject to interstate access charges, ride free, while the terminating carrier seeks reciprocal compensation for these "local" interstate calls.

All of these arrangements are different from foreign exchange ("FX") services that LECs have offered for many years. With FX service, the LEC actually has facilities and customers in

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11 *Investigation into Use of Central Office Codes (NXXs) by New England Fiber Communications LLC d/b/a Brooks Fiber Communications*, Order Requiring Reclamation of NXX and Special ISP Rates by ILECs (Order No. 4), Docket No. 98-758 (Me. P.U.C. June 30, 2000) (emphasis added) ("*Maine Order*").

12 *Id.* at 4. The transport involved in such schemes can be substantial. For example, in Maine if a carrier had purchased numbers in Presque Isle Rate Center in the north of the state, Verizon could have to haul a call from that area all the way to a switch in Portland, a distance of over 200 miles with no compensation for the service. *See* Attachment B (graphic). In contrast, if the called party is an ISP collocated with the carrier, then the carrier would incur little or no cost to complete the call.

13 *Maine Order* at 15.

14 *Id.*, and Order on Reconsideration (Nov. 14, 2000).

the exchange area for which it has received telephone numbers. Those carriers that use these schemes, however, ask for numbers for areas in which they have no plans to look for customers and no facilities with which to serve them if they did. Contrary to the claims of these carriers, these services are not just like ILEC FX services.[15] They are simply attempts to play games with the system.[16]

**The Abuse of Numbering Resources Scheme**. These arrangements waste increasingly scarce numbering resources, as they encourage LECs to obtain numbers in areas in which they will have no customers. This wastefulness contributes to the need to add new area codes, with resulting costs and confusion for carriers and consumers alike. And as long as the Commission permits compensation for Internet-bound calls, these arrangements increase the volumes of such calls and the resulting market distortions and inefficient behavior.

Such practices violate existing Commission regulations and industry numbering guidelines. Section 52.15(g)(2) of the Commission's rules allows a LEC to obtain telephone numbers if "the applicant is authorized to provide service in the area for which the numbering resources are being requested" and "the applicant is or will be capable of providing service within sixty (60) days of the numbering resources activation date." 47 C.F.R. § 52.15(g)(2).

[15] Unlike CLEC misuse of number assignments, ILEC FX services do not impose transport costs on other carriers. Rather, when a customer of a CLEC residing in the local service area to which the ILEC NXX is assigned calls an ILEC FX customer, the call is routed to the CLEC switch, and then returned to the ILEC switch in the same local service area. The ILEC then transports the call to the distant FX customer.

[16] For similar reasons, these CLEC arrangements are also different from those employed by CMRS providers because CMRS providers actually have facilities and customers in the areas for which the numbers are assigned.

The LEC must support its application with "documented proof" of these facts.[17] In particular, as to the second requirement:

> Carriers requesting initial numbering resources must also provide the NANPA appropriate evidence (*e.g.,* contracts for unbundled network elements, network information showing that equipment has been purchased and is operational or will be operational, business plans, or interconnection agreements) that its facilities are in place or will be in place to provide service within 60 days of the numbering resources activation date.[18]

In the circumstance described above, of course, the LEC was not capable of providing service in more than 50 rate areas for which it had obtained numbers, as it had no equipment or facilities in those areas.

The industry's NXX Assignment Guidelines, developed at the Commission's direction, contain similar requirements. They further provide that, "for assignment and routing purposes, the CO code (NXX) is normally associated with a specific geographic location within an NPA, from which it is assigned,"[19] are assigned "to the extent required to terminate PSTN traffic"[20] and "are assigned to entities for use at a Switching Entity or Point of Interconnection they own or control."[21]

The Commission should make it clear that LECs may not obtain numbers for use in this way.

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17 *Numbering Resource Optimization,* 15 FCC Rcd 7574 at ¶ 96 (2000).

18 *Id.* at ¶ 97.

19 CENTRAL OFFICE CODE (NXX) ASSIGNMENT GUIDELINES § 1.0 (June 11, 2001) *available at* http://www.atis.org/atis/clc/INC/Incdocs.htm.

20 *Id.* at § 4.1.

21 *Id.* at § 3.1.

**<u>The Reciprocal Compensation Scheme</u>**. The Commission also should make clear that LECs are not required to pay reciprocal compensation for these calls, either under existing rules or under any new intercarrier compensation regime.

Under the new reciprocal compensation order, the Commission reiterated that "both interstate and intrastate" calls that travel "beyond the local exchange" are excluded from reciprocal compensation requirements under the Act.[22] A call from one end of the State of Maine to the other — from Presque Isle to Portland — plainly is not within the "local exchange." The fact that the terminating carrier assigns a Presque Isle telephone number to its Portland customer does not change that fact.[23] Because these are, instead, interexchange calls, access payments would properly be due.

A number of state commissions have so held, finding that the terminating carrier was not entitled to compensation for these non-local calls. These states include Connecticut,[24] Illinois,[25]

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[22] *Remand Order* at ¶ 37.

[23] Similarly, where a customer dials an access code to reach an interexchange carrier which in turn connects the customer with the called-party, that is not a call within the local exchange, regardless of the location of the called party.

[24] "[T]he Department finds the carriers' requests for compensation in these cases disingenuous at best in light of the FCC and Department rulings (including defining their own local calling areas) and their ability to deploy facilities to make these calls truly local and eligible for mutual compensation. The purpose of mutual compensation is to compensate the carrier for the cost of terminating a local call and since these calls are not local, they will not be eligible for mutual compensation." *Investigation of the Payment of Mutual Compensation for Local Calls Carried Over Foreign Exchange Service Facilities*, Draft Decision, Docket No. 01-01-29, at un-numbered p. 21 (Conn. D.P.U.C. March 19, 2001).

[25] *TDS Metrocom, Inc., Petition for Arbitration of Interconnection Rates, Terms, and Conditions and Related Arrangements with Illinois Bell Telephone Co. d/b/a Ameritech-Illinois Pursuant to Section 252(b) of the Telecommunications Act of 1996*, Arbitration Decision, Docket no. 01-0338, at p. 48 (Ill. Comm. Comm'n August 8, 2001).

Texas[26] and Missouri.[27] The Commission, however, should not leave this problem to be resolved in multiple state proceedings. It should act now to clearly establish that its rules, both number administration and compensation, do not permit these arrangements and may not require the payment of local compensation for these calls.

C. Transport Issues Should Be Addressed More Immediately.

The Commission should also promptly resolve disputes under the current rules concerning transport costs.[28] These disputes have arisen when one LEC attempts to have another LEC bear transport costs that are beyond those recovered through the end user's local service rate design and that rightfully are the responsibility of the first LEC. The Commission should send the right signals to the market and encourage efficient interconnection by not placing unreasonable burdens on one interconnecting carrier as opposed to the other, by not allowing regulatory arbitrage and by not encouraging carriers to offer uneconomic services.

**2. Longer-Term Issues**

After resolving these near-term issues, the Commission should turn to what changes it should adopt in the various compensation systems and whether they should be replaced with a single system for all sorts of traffic. Before undertaking that inquiry, the Commission should clearly articulate what its goals are so that the proposals can be tested against those goals.

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[26] *Proceeding to Examine Reciprocal Compensation Pursuant to Section 252 of the Federal Telecommunications Act of 1996*, Arbitration Award, Docket No. 21982 at p. 17 (Tex. P.U.C. July 13, 2000).

[27] *Application of AT&T Communications of the Southwest, Inc., TCG St. Louis, Inc., and TCG Kansas City, Inc., for Compulsory Arbitration of Unresolved Issues With Southwestern Bell Telephone Company Pursuant to Section 252(b) of the Telecommunications Act of 1996*, Arbitration Order, Case No. TO-2001-455, at p. 27 (Mo. P.S.C. June 7, 2001).

[28] *Notice* at ¶¶ 112-14.

A. Guiding Principles

The Commission should base any new policies on the following principles.

**Minimize regulation.** The telecommunications marketplace is becoming more and more competitive every day. As a result, regulatory intervention is less and less required, and less and less appropriate. Intercarrier arrangements should be left, at the option of the parties, to private negotiation and agreement.

At the same time, regulation should establish default arrangements for those cases in which any party chooses not to negotiate an individual agreement, or in which the parties cannot agree. These default arrangements should be clear and self-executing, not requiring further involvement by the regulators.

Not only is clarity a desirable goal in its own right, the predictability that accompanies it will facilitate the negotiation process, as the parties will know for sure what the result will be if they cannot come to terms and will not see any benefit to rolling the dice in an arbitration or other regulatory proceeding. Without this clarity, the bargaining position of each carrier is determined in part by the carrier's expectations regarding the likely outcome of arbitration. If the expectations of the two parties differ, it is less likely that they will agree.

**Ensure competitive neutrality.** The starting assumption should be that the same rules apply irrespective of the technology used or the type of service provider involved. Differences in treatment should be based only on real technological or legal distinctions. The marketplace should decide which provider and what technology best meets individual customer needs. This decision should not be influenced by regulations that place burdens or costs on one provider or technology that competitive firms or technologies do not have to bear. Nor should the regulatory heritage of a service provider determine what rules it operates under; regulators should treat functionally competitive services the same, without regard to the identity of the entity that provides them. Therefore, regulatory distinctions should not be made, for example, simply on the basis of whether a transmission is circuit switched, packet switched or cell switched or whether the carrier is an ILEC, a CLEC, a DLEC or a CMRS provider. This does not necessarily mean, however, that the rules should ignore meaningful distinctions between technologies or providers. Nor does it mean that the same rules should apply to different types of services, for example, that the same compensation system should apply to both local calling and toll calling.[29]

It follows from this principle that the compensation system should allow consumers to compare price and service among competing providers. Allowing consumers to see prices that reflect all of the costs and benefits of each carrier's offerings would promote effective competition and consumer choice.

**Recognize past regulatory policies.** If the default compensation system eliminates an existing source of revenue (other than regulatory arbitrage) from a carrier, it must also offer the carrier another source to replace it. All carriers should have a reasonable opportunity to recover their actual costs. Carriers made investments with the perfectly reasonable expectation that regulators would allow them an opportunity to recover their costs. The Supreme Court has found that it raises "serious constitutional questions" if a regulator changes the rules in a way that deprives the carrier of that opportunity.[30] As the Court explained, when a ratemaker undertakes a fundamental shift in rate methodologies, the new methodology must be evaluated to

[29] There may be specific reasons to depart from consistent treatment in certain cases. For example, it is likely that exchange access service should be treated differently because of the magnitude of the revenues involved, the legacy network architecture designed around the existing charging system, the issues surrounding alternative recovery of those revenues, and the fact that authority for access is split between the Commission and state regulators.

[30] *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 315 (1989).

determine whether it continues to provide constitutionally adequate compensation for previous investments, as measured under the old methodology. While this is a matter of concern for all forms of traffic, the issue is particularly acute with respect to access, because of the significant proportion of costs recovered through access charges and because authority over access is split between state and federal regulators.

**Coordinate among the jurisdictions.** State and federal policies must be coordinated and consistent. Jurisdictional issues should be resolved at the outset. If the Commission is going to replace one source of cost recovery with another in pursuit of interstate intercarrier compensation reform, it is essential that any state actions be coordinated and consistent with the Commission's actions. Separate state and federal rules on architecture or compensation would undermine efforts to eliminate inefficient arbitrage.

**Promote economic efficiency.** Any new intercarrier compensation system should establish the correct incentives for both consumers and carriers to make efficient decisions. If not structured with care, a system that does not require one carrier to pay another for interconnection, transport or service can result in carriers behaving in ways that are economically inefficient, as price cannot act as a rationing mechanism.

Opportunities for inefficient arbitrage and gaming must be minimized or eliminated. This includes incentives to misreport or mischaracterize traffic and to change the classification of entities exchanging traffic (such as an end user "masquerading" as a carrier or vice versa). Additionally, an intercarrier compensation regime should avoid creating opportunities for one carrier to obtain service from another carrier without appropriate payment, under the guise of an interconnection arrangement.

Nor should one carrier be able to demand unreasonable interconnection arrangements that force another carrier to provide services without compensation. A local carrier in Illinois should not be required to carry traffic to another firm's switch in California in order to fulfill its obligation to interconnect. And a carrier should not be able to demand unique service quality without having to pay for it.

**Preserve universal service.** And, of course, any new compensation mechanism should not undermine the goals of universal service. Today, carriers receive significant revenues from intercarrier payments. This arose over time in part because of regulators' concerns about universal service. The system results in a particular payment pattern from end users with different services and usage patterns and using different carriers. A new framework, such as bill-and-keep, will produce a different distribution of payments by end users. While the new pattern may be desirable for many reasons, such as improved efficiency, it will change the amounts different customers pay. Thus, in adopting any new framework, the Commission must consider the possible effect new patterns of recovery will have on universal service.

B. Local Calls

The Notice has identified the various problems caused by the existing scheme of intercarrier compensation for local calls.[31] It also correctly notes that a pure bill-and-keep system could eliminate many of the complexities and issues raised by the existing system.[32]

The Commission's basic approach should be to let carriers, and the marketplace, work out mutually beneficial, efficient arrangements. It should not mandate one scheme for everyone.

It would, however, be appropriate for the Commission to adopt uniform default guidelines that apply in the event that parties do not negotiate alternative arrangements. These

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31 *Notice* at ¶¶ 17, 69.

32 *Notice* at ¶ 52.

guidelines should address the compensation plan, the location at which that system begins, and the related default architecture requirements. These guidelines should apply, whenever possible, to all service providers in order to maintain equal competitive opportunities and eliminate inefficient arbitrage opportunities.

If the Commission were to adopt bill-and-keep as the default compensation system, it would have to carefully write rules to prevent inefficient gaming and arbitrage and to ensure that one carrier cannot foist the costs it should properly bear onto another carrier. Issues that would need to be resolved include defining a central office (especially given the changing technologies and network architectures), distinguishing carrier networks from networks or switches of end user customers, the proper handling of one-way traffic and identifying the point at which a carrier transfers responsibility to a terminating or intermediate carrier's network.

Timing is also important. If bill-and-keep is going to be the default for local calls, that change should be done whenever bill-and-keep becomes the rule for Internet-bound calls.

C. Toll Calls and Access

The CALLS plan adopted by the Commission took effect only a year ago and will last until mid-2005. It establishes interstate access rate levels and an aggregate amount of interstate universal service support for 97 percent of the interstate access traffic. The Commission is correct that the question to be answered is, "What comes after CALLS?"[33] Thus, there should be no major changes in the CALLS plan until 2005.

Indeed, one of the objectives of the CALLS plan was to provide a five-year period of stability in the access rules. This would allow both LECs and interexchange carriers to plan more effectively and would put an end to the arguments over access rates that had occupied so

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[33] *Notice* at ¶ 97.

many resources since 1990. The Commission would violate its own commitment to stability if it were to reopen debate over access rate issues only a year after adopting CALLS.

Likewise, whatever new rules the Commission adopts in response to the Multi-Association Group ("MAG") plan should be given a chance to run their course before any fundamental change in the intercarrier compensation system. In addition, because it would be unsustainable for bill-and-keep to be the default rule in one ILEC territory but not in its neighbor's, any transition from access to something else must occur at the same time everywhere. Therefore, the question the Commission should answer is, "What comes after CALLS and MAG?"

At this point, it is far from clear whether the public would benefit from an elimination of the access charge regime — far more information is required before such a determination could be made. However, it is clear that the Commission would have to resolve numerous issues and make fundamental changes in existing rules before such a change could be made.

The states would also have to buy into the new plan and resolve issues consistent with the Commission's plan. Many of the benefits of bill-and-keep — simplicity, reduction of administrative burden, etc. — will be lost if there were inconsistent federal and state intercarrier compensation regimes. That situation would also create new opportunities for mis-reporting, gaming and arbitrage, which the *Notice* seeks to reduce.

Incumbent local exchange carriers today collect some $11 billion annually in interstate access charges from interexchange carriers. These revenues are used to cover these carriers' costs of providing service. If LECs cannot collect this money from interexchange carriers, the Commission must provide the opportunity for LECs to earn it from other sources.[34]

There are also a host of implementation questions that would have to be resolved before bill-and-keep could substitute for access. For example,

- The Commission would have to adopt rules defining appropriate default points of interconnection between LECs and interexchange carriers.
- In doing so, it must answer how large a geographic area can be served by a single point of interconnection. Compensation arrangements must be structured so that one carrier cannot transfer its own network costs onto a connecting carrier.
- If the Commission were to establish a certain type of switch as the default point of interconnection, it would also have to provide a strict definition of what exactly that switch represents.
- Any bill-and-keep system could provide opportunities for gaming. In particular, if "carriers" did not have to pay for certain types of transport, while "end users" did, it would cause some end users to try to masquerade as carriers to try to get the benefit of the better deal.

The Commission would have to work all this (and more) out before adopting a substitute system, not try to fix it up afterwards.

Two items in the *Notice* deserve special comment. First, paragraph 101 asks whether TELRIC should be the basis of any new access charge regime. The answer is that it should not — these charges should generate revenues sufficient to recover the costs of the carrier's actual network, as these are the only costs that send correct price signals to the market. TELRIC produces costs based on the forward-looking costs of a purely hypothetical carrier that always

[34] Similarly, to the extent the intrastate access charge regime is modified, carriers would have to have an opportunity to recover these revenues as well.

uses throughout its network the most up-to-date technology deployed in the most efficient network configuration.[35]

The Commission should not consider extending such a requirement to the access regime.[36] Access charges help recover an ILEC's own costs, not some hypothetical carrier with an optimal network. The FCC=s express goal in adopting TELRIC was to produce dramatically *lower* prices than would be dictated by either a measure of a carrier's actual forward looking costs or its historical costs.[37] Such a shift would be bad policy in that it would undermine future ILEC investment and, by underpricing the existing network, it would discourage competing investment as well. Moreover, under the Constitutional test set forth in *Duquesne Light Co. v. Barasch*, a new regulatory regime is unlawful if the new rates are not within the "range of reasonableness" based on the prior regime.[38] TELRIC cannot pass this test.

Since 1990, the Commission has relied on its price cap system to ensure that the amount of revenue LECs are allowed to receive through access charges is reasonable. If the Commission maintains access charges and continues price controls over them, it should continue to rely on the price cap mechanism. If, at the end of the CALLS plan, the Commission considers a

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[35] *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, 11 FCC Rcd 15499*, && 679, 683-685 (1996) ("*Local Competition Order*").

[36] Ironically, in the current Supreme Court review of TELRIC, the Commission has pointed to the relatively higher cost recovery allowed in regulated services (including access services) as justification for the imposition of TELRIC as the pricing standard for unbundled elements. Brief for Respondents FCC and United States at 34, *Verizon Communications v. FCC*, Nos. 00-511 et al., (U.S. filed June 2001).

[37] *Local Competition Order* at ¶ 706 (historical costs would require Aincreasing the rates for interconnection and unbundled elements")

[38] *Duquesne* at ¶ 312.

transition to bill-and-keep, then the price cap revenue under CALLS should become the basis for initializing the alternative end-user recovery mechanism that would replace access charges.

Second, paragraph 109 asks whether the existing rate structure should be changed, in particular to a capacity-based rate scheme. There is no need to establish new rate structures. What the Commission should be doing is eliminating rate structure requirements and providing increased flexibility to carriers. The idea of capacity-based pricing, as well as other alternative recovery structures, such as call set-up/duration and peak/off-peak pricing have been raised in other proceedings. Verizon and others demonstrated why these arrangements should not be required. The commenting carriers generally agreed that the costs remaining in the local switching category are traffic sensitive and that it was economic to recover these costs on a per-minute basis.[39]

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[39] *E.g.*, Comments of Bell Atlantic, *Access Charge Reform*, CC Docket Nos. 96-262 and 94-1, filed Oct. 29, 1999.

## Conclusion

The Commission should promptly deal with the three issues that need more immediate attention and carefully work through the much larger issues raised by any wholesale change in compensation mechanisms.

Respectfully submitted,

/S/

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ATTACHMENT A

## THE VERIZON TELEPHONE COMPANIES

The Verizon telephone companies are the local exchange and interexchange carriers affiliated with Verizon Communications Inc. These are:

Bell Atlantic Communications, Inc. d/b/a Verizon Long Distance
Contel of the South, Inc. d/b/a Verizon Mid-States
GTE Midwest Incorporated d/b/a Verizon Midwest
GTE Southwest Incorporated d/b/a Verizon Southwest
The Micronesian Telecommunications Corporation
NYNEX Long Distance Company d/b/a Verizon Enterprise Solutions
Verizon California Inc.
Verizon Delaware Inc.
Verizon Florida Inc.
Verizon Hawaii Inc.
Verizon Maryland Inc.
Verizon New England Inc.
Verizon New Jersey Inc.
Verizon New York Inc.
Verizon North Inc.
Verizon Northwest Inc.
Verizon Pennsylvania Inc.
Verizon Select Services, Inc.
Verizon South Inc.
Verizon Virginia Inc.
Verizon Washington, DC Inc.
Verizon West Coast Inc.
Verizon West Virginia Inc.

# The Maine Game